

SPECIAL FEATURE

Low-fare competition price effects

In past Special Features of this report, we have attempted to highlight the positive effect that low-fare competition has on fares. In most instances, we have either compared the distribution of actual fares paid before and after low-fare entry in a particular market or set of markets, or compared average fares in low-fare and non-low-fare markets to one another. In this quarter's Special Feature, we use the Standard Industry Fare Level (SIFL) as an objective benchmark against which to compare average fares paid in markets with and without low-fare competition.

With the deregulation of domestic air fares in 1978, the Airline Deregulation Act mandated that the Civil Aeronautics Board establish the Standard Industry Fare Level (SIFL), which was equivalent to the lowest unrestricted coach fare charged in each market under regulation. The SIFL, like regulated fares, is derived from a distance-based formula that the CAB adjusted on a biannual basis to reflect changes in airline operating costs. Before the CAB's domestic fare authority lapsed at the end of 1982, the SIFL cost adjustments were used to establish fare level changes that the airlines could implement without CAB approval.

The Department of Transportation has continued to update the SIFL on a biannual basis since the dissolution of the CAB. The Department and others have used the SIFL as a benchmark for comparing changes in post deregulation fares. More detailed information on the SIFL calculations can be found at <http://ostpxweb.dot.gov/aviation> under Domestic Aviation.

In order to compare average fares to SIFL, average fares and SIFL by distance block were calculated for three sets of markets: all top 1,000+ domestic city-pair markets, the subset of those markets that had low-fare competition¹, and the subset of markets within the top 1,000+ that did not have low-fare competition. The data for low-fare markets was then further broken down to isolate fare information from low-fare carriers only. The attached chart shows average fares for each of the market sets as a percentage of the corresponding SIFL measure. As we have observed in past Special Features, the presence of low-fare competition has an unmistakable impact on the average fare level. The difference is most notable in short-haul markets, where low-fare carriers have historically concentrated service.

When considering the aggregate of all top-1,000+ markets the following observations are made:

- In top-1,000+ markets up to 750 miles, average fares exceed SIFL by varying degrees. They range from 45% above SIFL (in the 0 to 250-mile range) to 6% above SIFL (in

¹ A low-fare market is defined as one in which a low-fare carrier transports at least ten percent of the Origin and Destination traffic. Low-fare carriers used in this comparison include: AirTran, American Trans Air, Frontier, Pro Air, Reno, Southwest, Spirit, Tower, Vanguard.

the 251-500 mile range).²

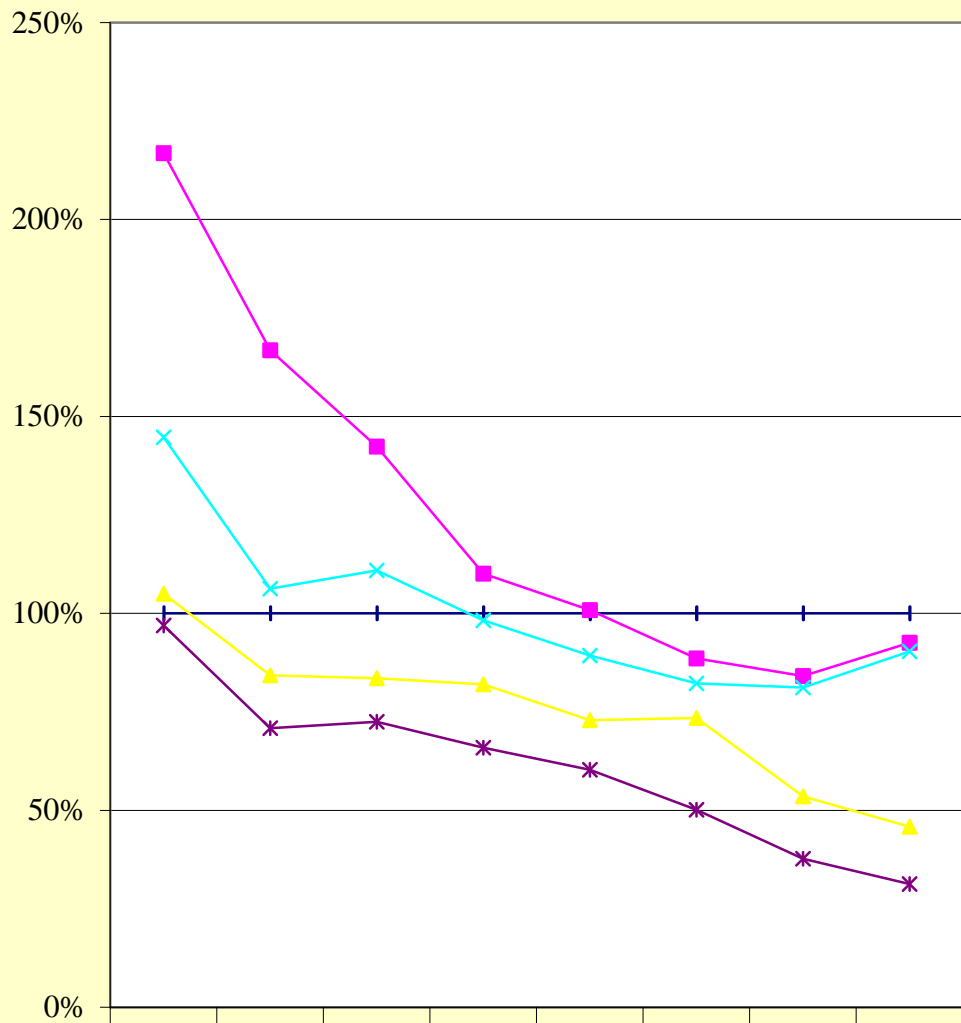
- In top-1,000+ markets over 750 miles, average fares fall below SIFL. They range from 81% to 98% of SIFL.

When the top-1,000+ markets are divided according to low-fare competition, however, different trends emerge:

- In markets with low-fare competition average fares were below the SIFL in all distance blocks with the exception of the under 250-mile block, where average fares were five percent higher than SIFL. In the two longest distance groupings, average fares were approximately half of SIFL.
- When the low-fare carrier data in low-fare markets is isolated, average fares fall even further below the SIFL. In the shortest distance block, fares charged by low-fare carriers are 97% of the SIFL. In the longest distance block, they are less than one-third of SIFL.
- In markets without low-fare competition, average fares in the shortest distance block were more than double the SIFL. Average fares were 67% and 42% above SIFL in the next two mileage blocks, respectively. Average fares in the remaining mileage blocks hover close to SIFL, ranging from ten percent above SIFL to 16 percent below.

² The components of the SIFL formula are uniformly adjusted to reflect overall changes in the level of operating costs, but not changes in the structure of airline operating costs. Airlines have had much greater freedom in managing costs since deregulation and the relative differences in the costs of operating short distance markets and long distances markets has likely changed.

**Average Fares Measured Against SIFL
Top 1,000+ U.S. Domestic Markets
Second Quarter 1998**



	Up to 250	251 - 500	501 - 750	751 - 1000	1001 - 1500	1501 - 2000	2001 - 2500	More than 2500
—+— SIFL	100%	100%	100%	100%	100%	100%	100%	100%
—■— Non-Low-Fare Mkts	217%	167%	142%	110%	101%	89%	84%	93%
—▲— Low-Fare Mkts	105%	84%	84%	82%	73%	73%	54%	46%
—×— All Mkts	145%	106%	111%	98%	89%	82%	81%	90%
—*— Low-Fare Carriers in Low-Fare Mkts	97%	71%	72%	66%	60%	50%	38%	31%

Distance Block